

(e) *Delay fee.* If, in the judgement of SBA, the time required to complete your examination is delayed due to your lack of cooperation or the condition of your records, SBA may assess an additional fee of up to \$500 per day.

[62 FR 23338, Apr. 30, 1997]

### Subpart G—Financing of Small Businesses by Licensees

#### DETERMINING THE ELIGIBILITY OF A SMALL BUSINESS FOR SBIC FINANCING

#### **§ 107.700 Compliance with size standards in part 121 of this chapter as a condition of Assistance.**

You are permitted to provide financial assistance and management services only to a Small Business. To determine whether an applicant is a Small Business, you may use either the financial size standards in § 121.301(c)(1) of this chapter or the industry standard covering the industry in which the applicant is primarily engaged, as set forth in § 121.301(c)(2) of this chapter.

#### **§ 107.710 Requirement to finance smaller enterprises.**

Your Portfolio must include Financings to Smaller Enterprises.

(a) *Definition of Smaller Enterprise.* A Smaller Enterprise means any small business concern that:

(1) Both together with its Affiliates, and by itself, meets the size standard of § 121.201 of this chapter at the time of Financing for the industry in which it is then primarily engaged; or

(2) Together with its affiliates has a net worth of not more than \$6 million and average net income after Federal income taxes (excluding any carry-over losses) for the preceding two years no greater than \$2 million. If the applicant is not required by law to pay Federal income taxes at the enterprise level, but is required to pass income through to its shareholders, partners, beneficiaries, or other equitable owners, the applicant's "net income after Federal income taxes" will be its net income reduced by an amount computed as follows:

(i) If the applicant is not required by law to pay State (and local, if any) income taxes at the enterprise level, multiply its net income by the mar-

ginal State income tax rate (or by the combined State and local income tax rates, as applicable) that would have applied if it were a taxable corporation.

(ii) Multiply the applicant's net income, less any deduction for State and local income taxes calculated under paragraph (a)(2)(i) of this section, by the marginal Federal income tax rate that would have applied if the applicant were a taxable corporation.

(iii) Add the results obtained in paragraphs (a)(2)(i) and (a)(2)(ii) of this section.

(b) *Smaller Enterprise Financings—(1) General rule.* At the close of each of your fiscal years, for all Financings you extended since April 25, 1994, excluding Financings made in whole or in part with Leverage in excess of \$90,000,000, at least 20 percent (in total dollars) must have been invested in Smaller Enterprises. If you were licensed after April 25, 1994, the 20 percent requirement applies to the Financings you extended since you were licensed, excluding Financings made in whole or in part with Leverage in excess of \$90,000,000, plus any pre-licensing investments approved by SBA for inclusion in your Regulatory Capital. For purposes of this paragraph (b)(1), Leverage in excess of \$90,000,000 includes aggregate Leverage over \$90,000,000 issued by two or more Licensees under Common Control. See also paragraph (d) of this section.

(2) *Phase-in for new Licensees.* At the close of your first full fiscal year after licensing, at least 10 percent of the total dollar amount of the Financings you extended, including any pre-licensing investments approved by SBA for inclusion in your Regulatory Capital, must have been invested in Smaller Enterprises. At the close of each fiscal year thereafter, you must meet the requirement in paragraph (b)(1) of this section.

(c) *Special requirement for certain leveraged Licensees.* (1) This paragraph (c) applies if you were licensed on or before September 30, 1996, and you issued Leverage after that date, and you have Regulatory Capital of:

(i) Less than \$10,000,000 if such Leverage included Participating Securities; or

(ii) Less than \$5,000,000 if such Leverage was Debentures only.

(2) At the close of each of your fiscal years, at least 50 percent of the total dollar amount of the Financings you extended after September 30, 1996 must have been invested in Smaller Enterprises.

(d) *Special requirement for Leverage over \$90,000,000.* If you have issued Leverage over \$90,000,000 (including aggregate Leverage over \$90,000,000 issued by two or more Licensees under Common Control), at the end of each of your fiscal years the cumulative Financings you extended to Smaller Enterprises must equal at least:

(1) The dollar amount necessary to satisfy paragraph (b) of this section; plus

(2) 100 percent of the amount of all Financings made in whole or in part with Leverage over \$90,000,000.

(e) Financing a change of ownership which results in the creation of a Smaller Enterprises. The Financing of a change of ownership under §107.750 which results in the creation of a Smaller Enterprise qualifies as a Smaller Enterprise Financing.

(f) *Non-compliance with this section.* If you have not reached the required percentage of Smaller Enterprise Financings at the end of any fiscal year, then you must be in compliance by the end of the following fiscal year. However, you will not be eligible for additional Leverage until you reach the required percentage (see §107.1120(c) through (e)).

[62 FR 11760, Mar. 13, 1997, as amended at 63 FR 5866, Feb. 5, 1998; 64 FR 70995, Dec. 20, 1999; 66 FR 30647, June 7, 2001]

**§ 107.720 Small Businesses that may be ineligible for financing.**

(a) *Relenders or reinvestors.* You are not permitted to finance any business that is a relender or reinvestor.

(1) *Definition.* Relenders or reinvestors are businesses whose primary business activity involves, directly or indirectly, providing funds to others, purchasing debt obligations, factoring, or long-term leasing of equipment with no provision for maintenance or repair.

(2) *Exception.* You may provide Venture Capital Financing to Disadvantaged Businesses that are relenders or

reinvestors (except banks or savings and loans not insured by agencies of the federal government, and agricultural credit companies). Without SBA's prior written approval, total Financings under this paragraph (a)(2) that are outstanding as of the close of your fiscal year must not exceed your Regulatory Capital.

(b) *Passive Businesses.* You are not permitted to finance a passive business.

(1) *Definition.* A business is passive if:

(i) It is not engaged in a regular and continuous business operation (for purposes of this paragraph (b), the mere receipt of payments such as dividends, rents, lease payments, or royalties is not considered a regular and continuous business operation); or

(ii) Its employees are not carrying on the majority of day to day operations, and the company does not provide effective control and supervision, on a day to day basis, over persons employed under contract; or

(iii) It passes through substantially all of the proceeds of the Financing to another entity.

(2) *Exception for pass-through of proceeds to subsidiary.* You may finance a passive business if it is a Small Business and it passes substantially all the proceeds through to one or more subsidiary companies, each of which is an eligible Small Business that is not passive. For the purpose of this paragraph (b)(2), "subsidiary company" means a company in which at least 50 percent of the outstanding voting securities are owned by the Financed passive business.

(3) *Exception for certain Partnership Licensees.* With the prior written approval of SBA, if you are a Partnership Licensee, you may form one or more wholly-owned corporations in accordance with this paragraph (b)(3). The sole purpose of such corporation(s) must be to provide Financing to one or more eligible, unincorporated Small Businesses. You may form such corporation(s) only if a direct Financing to such Small Businesses would cause any of your investors to incur unrelated business taxable income under section 511 of the Internal Revenue Code of 1986, as amended (26 U.S.C. 511). Your ownership of such corporation(s)